To avoid this, the Commission should adopt a complaint mechanism designed to identify only those cable operators charging egregious rates. Only by adopting such an approach, designed to catch the bad actors and otherwise create a safe harbor for all other cable operators, will the Commission ensure continued growth in the quantity and quality of programming.

C. To Catch "Bad Actors" Charging Egregious Rates for Cable Programming Services, The Commission Should Adopt an "Outlier" Approach To Identify Those Cable Operators Whose Prices Exceed an Established Industry Norm

Neither rate of return nor even a benchmark approach can satisfy the concerns identified above. Plainly, the best and most direct means of targeting the "bad actors" of the cable industry is by directly identifying a class which is likeliest to contain them. The Notice begins to suggest just such an approach by identifying current rates and targeting the top 2-5% of systems (or subscribers) as measured in terms of rate levels.[108] Rather than use this as a benchmark, however, the Commission should simply identify the "outliers" through this process. These companies would be thereafter subject to complaints, as set forth in subsection 623(c)(3). All other operators would be entitled to the safe harbor of the industry norm. As Dr. Kelley explains:

> Appropriate choice of the reasonableness cut-off point will allow the Commission to detect instances of apparently abnormally high rates without subjecting itself to an unmanageable flood of complaints.[109]

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[108] Notice at ¶ 46.

[109] Kelley at 38.

He thus endorses the 2-5% proposal as a reasonable cut-off point.[110]

The Notice correctly identifies a problem with deploying such an approach repetitively. Over time the measured rates would reflect responses to the regulatory regime rather than independent industry performance.[111] This "racheting down" of rates, carried to its logical extreme, would force rates below profit making levels, indeed, down to zero. Obviously, the use of the outlier approach needs to be adjusted for this phenomenon. To achieve the necessary adjustment, Time Warner proposes that the outlier analysis be performed in the first year on the basis of actual rates charged, but thereafter in subsequent years on the basis of industry rate increases (rather than the revised rates themselves). Apparently excessive increases will thereby be identified and vulnerable to complaint and rollback. Industry norm increases can be presumed reasonable and within the safe harbor. In this way, the industry will be able to incur additional costs for new programming and/or new systems architecture without the 'racheting down' effects and without the constraints of an inappropriate index.[112]

Operators whose rates have exceeded the safe harbor of the industry norm are subject to complaint. However, as explained by Dr. Kelley:

> As with the basic service benchmark process, individual cable systems must have the ability to make a showing that given

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[110] Id.

[111] Notice at ¶ 47.

[112] Dr. Kelley endorses this approach to outlier targeting, as well. Kelley at 38.

particular cost circumstances, their cable programming service rates are reasonable.[113]

Time Warner is especially concerned here with programming expenses, which constitute as much as 30% of the basic revenues of a typical cable system and which have been rising at extraordinary rates in the past few years along with entertainment costs in general.[114] In any given year, therefore, a dramatic increase in programming costs might very well cause a cable operator to exceed the safe harbor limits for cable programming service price increases. While most of the cost increases will be reflected in the selection of an appropriate index, this will not always be the case. Thus, in defending a complaint, "outlier" cable systems should be able to pass-through increased costs to demonstrate reasonableness.

Especially because Congress estimated that cable programming services face closer economic substitutes than does the basic "antenna service" tier, it is critical that the Commission establish and maintain a simple, minimally intrusive design for reaching the exceptional, unreasonable rates for such services.

D. The Procedures for Cable Programming Services Should Be Simple And Streamlined and Should Not Interfere With the Procedures Established By Local Franchising Agreements

The procedures which will govern cable programming services must similarly mesh with the minimal substantive regulatory approach to be taken there. For all cable operators whose rates fall within the safe harbor of the industry norms, the Commission must assure that the safe

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[113] Id.

[114] Id. at 26 and Exhibit II.

harbor remains safe. It should automatically dismiss any complaint regarding the rates of any cable system which lies within the norm. Any such complaint must be filed "within a reasonable period of time." This section, in effect, gives the Commission authority to establish an administrative 'statute of limitations' for purposes of these complaints.

The legislative history gives no guidance to the agency as to the length of time Congress deemed reasonable. However, a certain amount of guidance can be gleaned from the Act itself. The rate regulation provisions already require cable operators to provide 30-days notice for basic service tier increases. If a 30-day period is considered adequate notification time for the comprehensively regulated service, then plainly it should be deemed adequate for programming which is only regulated in the exception. Moreover, the complaint process mandated by Congress is deliberately streamlined to facilitate the filing of complaints without the need to hire an attorney,[115] thereby decreasing substantially the need for a lengthy period of time between notice and filing time. The only question which remains, then, is how to establish "notice" as the starting time for the 30 days. Time Warner respectfully submits that the time period should run from the time the Commission publishes its outlier analysis. This will establish which complaints are within the subject matter jurisdiction of the Commission.

Where a complaint is determined by the Commission to state a cause of action, the operator should have a comparable 30 day response time.

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[115] See Conference Report at 64.

The operator at that time should have the choice to realign its rates within the industry norm. Absent doing so, it must demonstrate just cause for the apparently high rates. These proceedings would be governed by the provisions of the Administrative Procedure Act. Similarly, access to confidential information could be governed by existing Commission rules providing for confidentiality orders.[116]

The Notice further proposes to find that the Commission has refund authority pursuant to Section 623(c)(1)(C), and seeks comment on how to implement such authority.[117] Where cable programming rates have been deemed unreasonable, "a prospective percentage reduction in the unreasonable service rate to cover the cumulative overcharge ... sent to the class of subscribers that had been unjustly charged"[118] appears to be the only workable type of refund that can be ordered on a system-wide basis.

V. REGULATION OF RATES FOR EQUIPMENT

The 1992 Cable Act establishes two distinct approaches for evaluating the rates charged by cable operators for various types of equipment provided to cable subscribers. Specifically, pursuant to Section 623(b)(3), the Commission's basic rate regulations are to include rate standards for "installation and lease of the equipment used by subscribers to receive the basic service tier," as well as "installation and monthly use of connections for additional television

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[116] See 47 C.F.R. §§ 0.457, 0.459, 0.460.

[117] Notice at ¶ 107.

[118] Id. at ¶ 108.

receivers" ["additional outlets" or "AOs."][119] Pursuant to Section 623(c), on the other hand, the Commission's regulations applicable to cable programming services (or "tiers") are to include "installation or rental of equipment used for the receipt of such video programming."[120] Equipment utilized solely to receive pay or a la carte services would remain outside either standard and would continue to be unregulated, with one minor exception discussed below.

A. Only Equipment Used Solely to Receive Basic Service is Regulated Based on Actual Cost Pursuant to Section 623(b)(3)

As the Notice correctly points out, the 1992 Cable Act clearly distinguishes between regulation of rates for equipment used to receive basic service and equipment used to receive cable programming services.[121] One key difference is that regulation of equipment used to receive basic service involves pricing based "on actual cost."[122] This criterion is designed to ensure that the rates for basic equipment are reasonable. Oversight of rates associated with cable programming service, including equipment used to receive such service, involves

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[119] 1992 Cable Act § 623(b)(3)(A),(B).

[120] Id. § 623(c)(2), (l)(2).

[121] Notice at ¶ 64.

[122] 1992 Cable Act § 623(b)(3). Pricing based on actual cost does, however, include a reasonable profit. See id. § 623(b)(2)(C)(vii); Conference Report at 63 ("The conferees agree that the cable operators are entitled to earn a reasonable profit.") The purpose of the "actual cost" basis "is to require cable operators to price these items fairly, and to prevent them from charging prices that have the effect of forcing subscribers to purchase these items several times over the term of the lease." House Report at 83-84. Stated otherwise, "cost" includes the cost of capital.

cost as only one of several factors to be considered.[123] These are precisely the same factors that the Commission must consider in evaluating complaints alleging that cable programming service rates are unreasonable. Unlike basic equipment regulation, the issue under Section 623(c) is whether the non-basic equipment rates are so egregious and out of range as to be found to be "bad actor" rates. In other words, the presumption is that the rates for cable programming service equipment are reasonable absent a finding that they fall within a narrow unreasonableness test designed to "rein in" a small class of outliers. Thus, the clear intent of the 1992 Cable Act is to provide two different approaches to rate scrutiny, based upon the type of service being provided, and to subject only equipment required solely to receive basic service to pricing based on actual cost.[124]

This intent to have different standards for basic, non-basic, and premium service-related equipment is further evidenced by an examination of Section 623(b)(3)(A) of the 1992 Cable Act, which specifies the two types of equipment that must be priced as basic equipment (i.e., based on actual cost): (1) equipment "used by subscribers to receive the basic service tier," and (2) "such addressable converter box or other equipment as is required" for a

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[123] 1992 Cable Act § 623(c), (1)(2). Of course, another crucial difference is that regulation of cable programming service takes place at the Commission level, and only upon a valid complaint of unreasonable rates from a subscriber or relevant state or local government authority. Id. at § 623(c)(1), (2).

[124] Dr. Kelley makes this point, as well: "Following the logic of the rationale for basic service regulation, only that equipment that is necessary for receipt of basic channels need be subjected to rate regulation." Kelley at 13.

basic-only subscriber to receive programming on a per channel or per program basis pursuant to Section 623(b)(8) of the 1992 Cable Act (i.e., without being required to "buy through" intermediate service tiers).[125] If Congress intended all equipment to be priced based on actual cost, there would have been no need to specify that rates applicable to descrambling equipment used to receive pay services by a basic-only subscriber should be reviewed on the basis of actual cost, because such equipment would have been included. Rather, Congress must have intended that equipment used to receive premium service as well as basic service, except in the limited situation of a basic subscriber receiving pay services without intervening non-basic tiers and taking advantage of the 1992 Cable Act's anti buy-through provisions, need not be evaluated on the basis of actual cost. There is simply no other logical way to read the foregoing provisions of the 1992 Cable Act.

It should be noted that the change in language regarding equipment rate regulation between the original House bill (which dealt with "equipment necessary for subscribers to receive the basic service tier")[126] and the 1992 Cable Act (which mentions "equipment used by

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[125] 1992 Cable Act § 623(b)(3)(A)(emphasis added). Time Warner notes that the 1992 Cable Act's use of the term "addressable converter" here is a misnomer. "Converters" are units attached to a subscriber's television set that provide expanded bandwidth, thereby enabling the television to receive programming transmitted along higher frequency bands. In essence, these converters act as supplemental "tuners" for the television set. "Addressable" or "Programmable" boxes, on the other hand, are more sophisticated units used to secure programming by employing scrambling/descrambling techniques.

[126] See House Report at 83.

subscribers to receive the basic service tier")[127] is not substantive. Rather, the change was made for two reasons: (1) to mirror the equipment language included in the 1992 Cable Act's "cable programming service" definition ("equipment used for the receipt of such video programming"),[128] and (2) to "give[] the FCC greater authority to protect the interests of the consumer."[129] There is no evidence to suggest the revision was made to mandate an interpretation which would potentially expose the vast majority of the equipment offered by cable operators to the actual cost standard. First, virtually all cable equipment is capable of receiving signals for basic, non-basic, and pay programming. Second, in answer to the Notice's question whether equipment exists that is designed to receive only certain types of programming, such as non-basic,[130] there simply is little or no such equipment on the market, nor has there ever been in an environment of multi-tier offerings. Such a situation would require that multiple addressable boxes be placed in the homes of subscribers to multiple service tiers -- a very expensive and very consumer unfriendly consequence.

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[127] 1992 Cable Act § 623(b)(3)(A).

[128] Id. § 623 (1)(2)(emphasis added). As the Commission notes at n. 94 of the Notice, Congress added installation and equipment to Section 623(c) at the same time that it changed "necessary" to "used" in § 623(b)(3). Again, this demonstrates that Congress merely was attempting to harmonize these two sections.

[129] Conference Report at 64.

[130] Notice at ¶ 65.

There is, moreover, precedent from the Commission and the U.S. Copyright Office for distinguishing among equipment offered by cable operators to subscribers, based on the type of service being subscribed to. For example, in a 1989 letter, the U.S. Copyright Office addressed a situation where a cable operator offers two levels of service, such as a limited basic containing all broadcast signals and an optional expanded tier of service. A simple box was provided to the basic-only subscribers at a $1.00 monthly rental. A more sophisticated addressable box was provided to the expanded tier customers at a $3.00 monthly rental. The Copyright Office ruled that only the $1.00 rental fee need be included in gross receipts attributable to basic service for copyright purposes, not the full $3.00 charge for the expanded tier addressable box, even though expanded tier customers also received the basic level signals as part of their overall package and such signals were processed by the $3.00 addressable box.[131] Similarly, the Commission, in cases holding that cable operators could not charge for addressable boxes needed to receive must-carry stations, clearly distinguished between equipment used to receive basic service and equipment used to receive non-basic (cable programming) service.[132]

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[131] Letter from Dorothy Shrader, General Counsel, U.S. Copyright Office, to James F. Ireland (Oct. 11, 1989)(on file with the U.S. Copyright Office).

[132] See Cablevision, Inc. (Alma, Mich.), 48 Rad. Reg (P&F) 2d 1401 (1981)(cable operator repositioning of must carry channel "to a second tier cable channel" requiring an addressable box for reception violated must carry rules); Clear Television Cable Corp. (Berkley Twp., N.J.), 46 F.C.C.2d 744 (1974); Columbia Television Company, Inc. (Pendleton, Or.), 42 F.C.C.2d 674 (1973).

Accordingly, the Commission should clarify that the capacity for cable equipment to receive non-basic and pay as well as basic programming cannot determine how it is regulated. Rather, the service level of the subscriber using particular equipment should determine its level of regulatory scrutiny. Thus, only equipment used solely to receive basic service should be subject to pricing based on actual cost. If equipment (such as a remote control) is not even offered to a basic-only subscriber, then it obviously cannot be deemed "used to receive basic service" and thus would not need to be priced based on actual cost. Rates or charges for equipment used by subscribers to receive cable programming services should be analyzed under Section 623(c), concerning unreasonable cable programming service rates. Equipment used for services that are neither basic nor cable programming services (i.e., "per channel," "per program," or "pay" services), should not be subject to any rate regulation, because such services are themselves exempt from rate regulation.[133]

Similarly, if the same equipment (such as a remote control) that is offered to basic subscribers is also offered to and used by subscribers to receive higher levels of service, the equipment rate charged to the non-basic subscribers should be subject to non-basic rate standards contained in Section 623(c), or no regulation at all, depending on whether cable programming services or pay services were being subscribed to. For example, if the subscriber needs an addressable box to descramble tier service, the Section 623(c) rate

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[133] See 1992 Cable Act § 623(l)(2)(definition of "cable programming service" excludes "video programming carried on a per channel or per program basis").

regulation standard for cable programming services would apply. If, however, the subscriber uses the addressable box only to receive a pay programming tier, the device would not be subject to any rate regulation. Unless this distinction is maintained as to equipment common to different levels of service, Congressional intent would be thwarted.[134]

A simple analogy is illustrative here. When a subscriber selects an expanded service package from the cable operator, the subscriber will also receive the basic service level. This fact, however, does not require the entire service package to be regulated under the basic rate formula -- only the basic level is subject to basic rate regulation.[135] Likewise, the fact that equipment provided to subscribers to receive cable programming service or pay services also contains the capability of delivering basic service does not mean that the equipment is subject to the actual cost test applied to basic service equipment. Cable operators and other equipment marketers should remain free to offer equipment that, for reasons of technical superiority, consumer friendliness, or otherwise, combines the capacity to receive different types of programming, without the heavy hand of "actual cost" regulation hanging above.

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[134] In requiring that basic rates be "low," Congress has apparently anticipated that revenues from equipment used to receive non-basic or pay services might be used to subsidize rates for equipment used to receive basic service. See Conference Report at 63.

[135] See 1992 Cable Act § 623(b)(1). In fact, the Commission concludes in the Notice that the 1992 Cable Act's definition of "basic service" contemplates only a single tier. Notice at ¶ 13.

In addition to the foregoing legal arguments, there are technical reasons which support the above-listed distinctions between equipment used to receive basic service and equipment used to receive cable programming service. Basic service is almost universally offered on an unscrambled basis, thereby allowing access to that tier without the need for any terminal equipment, except in cases where the basic tier extends beyond the VHF band and a subscriber's television set is not equipped to receive these higher band signals. In these limited cases, the converters provided to basic subscribers are relatively inexpensive boxes which are nothing more than extended tuners and are similar to the tuners which are built into certain television sets. Accordingly, such equipment falls within Section 623(b)(3).

In contrast, addressable boxes which are used to receive cable programming services, premium services, and pay-per-view services provide sophisticated electronic technology and signal security features, such as descrambling, channel mapping, etc., which go beyond the simple tuner extension function of those converters which, in a few instances, may be used exclusively in connection with the receipt of basic service. Although the basic services may pass through addressable boxes along with cable and premium services, this is merely a consumer-friendly convenience which avoids the need of providing an A/B switch and, in some cases, a second set top converter. Such basic services do not utilize or require the sophisticated descrambling/addressability features which are often incorporated into the devices which are used to provide tiers of cable service over and above the basic service. In short, an addressable box is not "used by

subscribers to receive the basic service tier" in any situation where the basic service channels are not scrambled.[136]

Accordingly, the equipment price charged to basic-only subscribers can and should be distinguished from the equipment price charged to non-basic or pay subscribers who receive cable programming or pay programming services in addition to basic service, even where the same equipment can perform all three functions. Specifically, the addressable box is to be reviewed under either the "bad actor" standard for cable programming services[137] or completely deregulated, depending on whether cable programming services or pay programming services are being scrambled.

B. Equipment Rates Should be Deregulated if Competition from Independent Suppliers Exists

The 1992 Cable Act expresses an overriding preference for competition over regulation.[138] Indeed, the statute includes an appropriate test to measure effective competition as to the service components of a cable operator's offerings.[139] However, the 1992 Cable Act's definition of "effective competition" is limited to the service components only and fails to address equipment, installation, and AOs.[140] Thus, since the 1992 Cable Act contains no parallel test regarding equipment, the Commission is free to adopt such a test.

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136 1992 Cable Act § 623(b)(3).

137 Id. § 623(c) and discussion supra, sections IV. A-B.

138 See 1992 Cable Act § 2(b)(2).

139 Id. § 623(l).

140 See id. § 623(l)(1).

Furthermore, the Commission is required to minimize the burdens on the agency, cable operators, franchising authorities, and subscribers in developing a basic rate regulation framework.[141] Establishing a standard by which rates for basic equipment can be totally deregulated is wholly consistent with this requirement. Deregulation of rates for equipment, installations, and AOs in such instances would further the policy of the 1992 Cable Act to "rely on the marketplace, to the maximum extent feasible."[142] Continuing to regulate such services and equipment, in the face of competition, on the other hand, would violate this stated policy.

In establishing an "effective competition test" for equipment, the Commission should keep in mind the statute's requirement that the Commission "promote the commercial availability, from cable operators and retail vendors that are not affiliated with cable systems, of converter boxes and of remote control devices compatible with converter boxes."[143] Thus, the test adopted by the Commission should be consistent with this statutory goal. Specifically, if the cable operator certifies that a particular piece of equipment is available for sale or lease from third party sources, and has so advised its subscribers, the price for that equipment should be deregulated.[144] Not only would such a test be wholly consistent with Congressional

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[141] Id. § 623(b)(2)(A).

[142] Id. § 2(b)(1), (2).

[143] Id. § 623A(b)(2)(C).

[144] Obviously, a cable operator making such a certification regarding remote control equipment would be precluded from taking actions to disable commercially available remote control units.

intent as explained above, it also would be fully consistent with the certification procedures in the 1992 Cable Act's basic rate regulation provisions.[145]

C. Rate Setting Issues

The 1992 Cable Act and the questions raised in the Notice lead to various rate setting issues regarding equipment, including the meaning of "on the basis of actual cost," the ability of cable operators to bundle rates for equipment and installations, and the regulation of rates for additional outlets. First, as was partially explained in footnote 122, supra, evaluating the pricing of cable equipment "on the basis of actual cost" includes the cost of capital, that is, Congress specifically provided for cable operators to earn a reasonable profit. Congress also specified that, in providing for the regulation of rates for the installation and lease of the equipment necessary for subscribers to receive basic service, "[t]he term 'actual cost' is intended to include such normal business costs as depreciation and service."[146] Moreover, the Commission correctly expresses concern that cable rates not be confiscatory, i.e., regulated at a price so low that cable operators cannot even cover their costs.[147] Accordingly, rates for the installation and lease of basic equipment must account for the following: installation, amortization, maintenance, financing, general administrative overhead, plus a reasonable profit. These are the basic

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[145] See 1992 Cable Act § 623(a)(2) - (a)(4).

[146] House Report at 83.

[147] See Notice at notes 66 and 79; 138 Cong. Rec. S.14583 (daily ed. Sept. 22, 1992)(statement of Sen. Lieberman).

costs associated with providing basic equipment and AOs, and thus were fully intended by Congress to be included in the basic equipment rate.

1. The Commission Should Permit Bundling of Equipment Rates

The Commission "tentatively conclude[s] that Congress intended to separate rates for equipment and installations from other basic tier rates."[148] While the separate tests established for the service and equipment components of basic service might suggest an effort to unbundle service from equipment, neither the 1992 Cable Act nor its legislative history evidences an intent to prohibit "bundling" in any form of various equipment components. Thus, for example, the Commission should not prohibit a bundled rate for addressable boxes (or converters) and remotes provided to subscribers. These two pieces of equipment are really two parts of one functional unit. The box receives the signals from the cable system and delivers them to the television set, while the remote permits the subscriber to access the television set to select among such signals. The remote sends an infrared signal which must be received and processed by the box. One piece will not work without the other. Moreover, viewed separately, the price for remotes might be relatively low (e.g., $15-$25+), while addressable box prices can be relatively high (e.g., $110-$150+). The only sensible way to account for both the wide price difference between addressable boxes and remotes, and the fact that they form a single functional equipment unit is to permit bundling of the equipment rate.

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[148] Notice at ¶ 63.

Such rate, moreover, needs to reflect the short useful life, rapid obsolescence, and high rate of churn associated with such equipment.

2. Installation Issues

Installation is another area where the Notice raises several important issues. The Commission recognizes in the Notice that "[m]any operators charge less than actual costs for service installation as part of their marketing efforts."[149] In fact, this is almost always the case. Installations are extremely costly, requiring considerable labor and "truck rolling," in addition to the cost of the wiring, equipment, etc. used in the installation. Similarly, cable operators commonly price subsequent service calls well below cost, or even free. It would contravene Congressional intent to preclude this flexibility for cable operators, which, as the Notice recognizes, can result in significant advantages for consumers by increasing cable penetration.[150] Such flexibility, therefore, should continue to include the unrestricted ability of cable operators to offer promotional discounts on installations as a mechanism to increase subscriber base.

Accordingly, cable operators should be allowed to establish hourly installation rates to account for unique circumstances, including local labor costs, etc., which can vary widely. Installation rates should be subject to a reasonableness standard, whereby the rate would be deemed reasonable if no greater than the hourly installation rate charged by the local exchange telephone carrier ("telco") that provides service in

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149 Id. at ¶ 70.

150 Id.

the area.[151] Such a standard should provide an adequate check against unreasonable installation rates, given that telephone installations require comparable trucks, equipment, skill levels, etc.

Moreover, as is the case with boxes and remotes, installation rates should also be deregulated if the cable operator's installation service is subject to "effective competition." Cable installation should be deemed subject to effective competition, and thus rate deregulated, if the operator allows subscribers to choose one of the following two options:

(1) payment of the full cost of installation up front, subscriber thereafter responsible for full cost of maintenance; or

(2) installation provided below cost, cable operator agrees to maintain inside wiring for a monthly charge no greater than 25% of the basic service rate.

The Notice also asks whether there should be a surcharge over the normal installation rate when the distance between a customer's premises and the operator's distribution plant is substantial.[152] Such situations are encountered frequently in the cable industry and fall into two general categories. One general category arises in situations where the cable operator's activated plant does not "pass" one or more homes within the franchise territory. Such situations are typically dealt with through a "line extension policy" whereby such subscribers might be required to advance a grant in aid of construction before service is provided. The other general category arises where the cable

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[151] See Kelley at 36.

[152] Notice at ¶ 70.

plant passes a given home, but the home is set back an abnormal distance from the street. In such cases, a "non-standard" installation rate is typically assessed over and above the standard fee. Time Warner's proposal that installation rates be deemed reasonable so long as they do not exceed the hourly rate allowed for the local telco would ameliorate at least the "non-standard" installation problem. But there is no reason why cable operators should not continue to be allowed to follow written line extension or non-standard installation policies, particularly if set forth in the franchise contract. Such an approach would be consistent with the "grandfathering" concept embodied in Section 623(j).

3. Additional Outlets

The Notice correctly recognizes that Congress intended to treat additional outlets the same as other equipment, "conclud[ing] that cable operators should use the same cost methodology they use for installation of other equipment to calculate the rates for installation of connections for additional receivers."[153]

Installation and maintenance of AOs is essentially similar to installation and maintenance of the initial subscriber drop, but it requires additional equipment and labor to connect AOs once the initial connection to the home is made. Accordingly, installation and maintenance of basic AOs should be regulated the same as the initial drop, as discussed above. First, the cable operator should be allowed to establish a reasonable hourly rate not exceeding that of the local telco. Again, promotional discounts should be permitted. Second, the

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[153] Id. at ¶ 71 (footnote omitted).

installation and maintenance of AOs should be deemed subject to "effective competition" under the Act where the cable operator offers subscribers the two options discussed above regarding the responsibility to pay full maintenance costs for internal wiring or a service contract approach.

Section 623(b)(3) of the 1992 Cable Act only addresses the equipment component of AOs (i.e., installation and monthly maintenance). This subsection does not address the service component of AOs, which comprises a much greater portion of the typical charge. Thus, in addition to the proper standard for scrutinizing installation and monthly maintenance of AO equipment, the Commission needs to address the appropriate standard for the service aspect of AOs.

The service component of AOs is governed by Section 623(b)(1) and (2) of the 1992 Cable Act regarding rate regulation of cable service generally. As was discussed in Section V. A. supra, the type of regulation of the AO service component would depend on the level of service being provided to the particular AO. Such service level could, of course, vary even within a single home, where it is not uncommon, for example, to have the initial drop in the living room receive a full array of tiered service, but the AOs in the bedrooms receive only basic service. Moreover, depending, of course, on the level of service provided, each AO is just as valuable as the first set because two residents of the same household can view different programming simultaneously. Thus, a cable AO is far different from an extension telephone, which only allows one conversation (unless the telephone subscriber pays for additional lines).

4. The Commission Should Permit Bundling of Equipment and Installation Rates

The Notice erroneously "tentatively conclud[es] that, to be consistent with the statute's intent, the rates for installation should not be bundled with rates for the lease of equipment."[154] As explained above, there is no Congressional intent to prohibit bundling of equipment.[155] Indeed, the 1992 Cable Act deals with equipment used to receive basic service in the same sentence and applies the same test.[156]

The Commission's sole rationale is "that this unbundling could help to establish an environment in which a competitive market for equipment and installation may develop."[157] There is no evidence, however, that a competitive environment for equipment and installation would be hindered by permitting cable operators to bundle equipment and installation rates. For example, a stroll down the aisle of Radio Shack or other electronics retailers demonstrates that a thriving industry for many different types of equipment, including A/B switches and remote control units, already exists. There is no reason to believe that such an industry, including installations, will not continue to develop. If bundling of equipment were prohibited, on the

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[154] Id.

[155] Similarly, nothing in the 1992 Cable Act prohibits the bundling of tiers of "cable programming service" with the equipment used to provide such service. See 1992 Cable Act § 623(l)(2).

[156] Id. § 623(b)(3).

[157] Id.

other hand, cable operators would face an unnecessary intrusion into their business practices.

Even if "bundling" of basic service and basic equipment were prohibited, the Commission should, at the very least, allow cable operators to establish their own rates for basic equipment, installation, service calls, and AOs, so long as such rates remain within a reasonable rate "pool."[158] Such an approach would allow the great majority of cable operators, who charge less than cost for installations and service calls, to recover those costs as part of the monthly rates for converters, remotes, or AOs. Consumers certainly would not be disadvantaged, because they would naturally be concerned chiefly that the amount of their monthly bill is reasonable, regardless of a change in allocation of costs among various elements of the bill. Moreover, a pool approach actually benefits consumers, since it does not foreclose cable service to members of the public who would decline service if a huge up front payment for each component of equipment, including installation, had to be priced at cost. The Commission may wish to undertake a special proceeding to determine the appropriate pooling parameters. Thereafter, as long as the cable operator's total basic equipment revenue was within the limits of the pool, its individual equipment rates would be deemed reasonable.

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[158] The Commission touches upon this issue in the Notice, asking, for instance, "whether the actual cost provision of the statute is contravened if individual promotions do not fully recover costs as long as provision of equipment in general does recover 'actual costs.'" Notice at ¶ 70.

VI. CUSTOMER CHANGES

Under Section 623(b)(5)(C), the Commission is instructed to promulgate standards to govern changes in service or equipment selection "subject to regulation under this section." The first question that arises under this section is whether this language extends to cable programming services, including the equipment used for the receipt of such programming, even though such services and equipment are not directly regulated. As discussed earlier, only rates for such services and equipment which are "unreasonable" are regulated under Section 623(c).[159] Rates within the safe harbor are not "subject to regulation" and thus, in general, charges for changes at this level should remain outside this provision. Under this construction, a "bad actor" which charges unreasonable rates for expanded tier(s) may also be subject to refunds for practices relating to charges for changes to these services. Otherwise, cable operators may assess charges for changes between and among expanded tier(s) and premium programming (and equipment relating to the same) free of regulation.

As to charges assessed for changes to or from the basic service tier, or changes subject to regulation under the "bad actor" provisions, the statute commands that such charges be "based on the cost of such change."[160] Where such change involves a house visit (to remove or insert a trap, for example), the operator is free (as it must

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[159] Plainly, rates for changes involving exclusively pay programming and related equipment are outside the scope of this section and the Commission's jurisdiction.

[160] 1992 Cable Act § 623(b)(5)(C).

be) to recover that not insubstantial expense.[161] The Commission should utilize the data it will develop with respect to installation charges to gauge the approximate direct cost of such a visit. Where such changes can be accomplished solely via computer entry, the section specifies a "nominal amount" to be charged.

The Notice correctly observes that there are indirect costs to high churn which are just as real as the direct costs involved in house visits.[162] Planning requires some stability in customer selection; the costs of inaccurate planning are necessarily shared by both the cable company and its customers. Cable operators should therefore be allowed to assess charges which contain some amount sufficient to discourage wholly arbitrary, continuous changes by subscribers. For example, it should be readily permissible that the charges escalate if a particular subscriber orders multiple changes within a certain period of time. Similarly, the nominal amount itself, even for the first change, should reflect some of the indirect costs of churn.

Finally, because this section was directed by Congress at those excessive charges being imposed as a means of discouraging cable subscribers from downgrading service,[163] a charge which is the same for

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[161] See House Report at 84 ("In some cases, the technical configuration of cable systems will be such that the selection back and forth between basic service and tiers offering cable programming may require equipment and labor costs to be incurred by cable operators. In such cases, reasonable charges or fees, based on actual costs, should be permitted.").

[162] Notice at ¶ 76. The Notice also correctly notes that charges for customer changes which are too low would require that cable operators' costs to implement these changes would have to be recovered from higher charges in other services. Id.

[163] See House Report at 84.